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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

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UNITED STATES BANKRUPTCY COURT

EASTERN DISTRICT OF CALIFORNIA

In re:) Case No. 05-22777-D-7

MELANIE HUGHES,)

Debtor.)

CLAYEO C. ARNOLD and CLAYEO
ARNOLD, PROFESSIONAL LAW
CORPORATION,)

Plaintiffs,)

v.)

MELANIE HUGHES,)

Defendant.)

Adv. Pro. No. 05-2225-D
Docket Control No. HSM-2

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MEMORANDUM DECISION

On May 22, 2007, Defendant Melanie Hughes filed a Motion for Summary Judgment, bearing Docket Control No. HSM-2 (the "Motion").¹ For the reasons set forth below, the court will deny the motion.

/ / /

1. On the same date, Plaintiffs Clayeo C. Arnold and Clayeo Arnold, Professional Law Corporation, filed a Motion for Partial Summary Judgment. That motion is under submission.

On March 14, 2005, Defendant Melanie Hughes (the "Debtor") filed a petition for relief under chapter 7 of the Bankruptcy Code. On June 14, 2005, Clayeo C. Arnold and Clayeo Arnold, Professional Law Corporation ("Plaintiffs"), initiated the above-captioned adversary proceeding. In the first and second causes of action set forth in their Complaint to Determine Dischargeability of Debts and for Denial of Discharge (the "Complaint"), the Plaintiffs contend that the Debtor made certain "false and baseless allegations against Plaintiffs arising out of her employment as a law clerk/secretary during the years 1994 through 1996." See Complaint, General Allegations, ¶ 1. The Debtor is alleged to have made these allegations in the course of a state court action, Rieger v. Arnold, et al., Sacramento County Superior Court Case No. 97AS03390.² That action resulted in a \$15,000 jury verdict in favor of the Debtor and against Arnold's law corporation on one of the Plaintiff's sexual harassment claims.

However, the trial judge ordered that the Debtor recover nothing from the Plaintiffs, notwithstanding the verdict, and proceeded to consider the motion of Arnold and his law corporation for an award of attorney's fees and costs, pursuant to Cal. Gov't Code § 12965(b). The court found Arnold and the law corporation to be the prevailing parties in the action, and made the following awards: to Arnold, \$66,213.50 in attorney's fees and \$265 in costs; to the law corporation, \$89,302.75 in

2. The Debtor previously went by the name Melanie Rieger.

1 attorney's fees and \$19,626.05 in costs. (These awards will be
2 referred to collectively as "the attorney's fee award.") The
3 state court's judgment was appealed, but is now final.

4 The Plaintiffs allege in the Complaint that as of March 14,
5 2005, Arnold was owed \$100,227.72 on the judgment, and the law
6 corporation, \$153,105.13. In their first and second causes of
7 action, the Plaintiffs allege that the Debtor prosecuted the
8 state court action "deliberately and intentionally to cause
9 injury" to the Plaintiffs, and that the attorney's fee award is
10 therefore nondischargeable, pursuant to 11 U.S.C. § 523(a)(6).

11 In their third and fourth causes of action, the Plaintiffs
12 seek to deny the Debtor's discharge, pursuant to 11 U.S.C. §
13 727(a)(3) and (a)(2)(A), respectively, on the grounds that the
14 Debtor has failed to keep or preserve books and records from
15 which her financial condition or business transactions might be
16 ascertained, and that she has, with intent to hinder, delay, or
17 defraud creditors, concealed property, within the year preceding
18 the filing of her bankruptcy petition. The facts underlying
19 these two causes of action will be further explored below.

20 On July 22, 2005, the Debtor filed a motion to dismiss the
21 Complaint for failure to state a claim. The motion was denied,
22 and on September 9, 2005, the Debtor filed an answer to the
23 Complaint.

24 With the Motion, the Debtor filed a number of exhibits, a
25 memorandum of points and authorities, declarations of Melanie
26 Hughes (the Debtor), Marc Hughes, and Thomas P. Griffin, and as
27 required by Local Bankruptcy Rule 7056-1(a), a separate statement
28 of undisputed facts. In the Motion, the Debtor seeks summary

1 judgment in her favor on all four of the Plaintiffs' causes of
2 action, but also asks the court to abstain from determining the
3 issues raised by the fourth cause of action.

4 On June 6, 2007, the Plaintiffs filed opposition to the
5 Motion, together with exhibits, a declaration of Clayeo C.
6 Arnold, and a response to the Debtor's separate statement of
7 undisputed facts. On June 7, 2007, the Plaintiffs filed certain
8 exhibits under seal, pursuant to this court's December 22, 2006
9 order on a discovery motion brought by the Plaintiffs (DCN No.
10 ARP-1).

11 On June 13, 2007, the Debtor filed a reply to the
12 Plaintiffs' opposition, together with additional exhibits and
13 another declaration of Melanie Hughes.

14 On June 20, 2007, the Motion came before the court for
15 hearing, counsel appeared and presented oral argument, and the
16 matter was submitted.

17 As to the Plaintiffs' first and second causes of action, the
18 Debtor argues generally that the attorney's fee award is
19 dischargeable because it was compensatory in nature, was not tied
20 to a judgment for an intentional tort, and is not binding on this
21 court on the issue of willful or malicious injury on the part of
22 the Debtor.

23 The Plaintiffs respond that the Debtor's conduct in
24 prosecuting her sexual harassment claims against them was willful
25 and malicious, that such conduct directly caused injury to the
26 Plaintiffs, in the form of the attorney's fees and costs they
27 expended in defending themselves, that the state court judge's
28 written findings in his order on the Plaintiffs' motions for

1 attorney's fees and costs are preclusive in this court, but that
2 if the state court's remarks are *dicta*, and the order therefore
3 not binding on this court, there remain genuine issues of
4 material fact that preclude summary judgment for the Debtor.

5 As to the Plaintiffs' third and fourth causes of action, the
6 Debtor argues essentially that the facts support her version of
7 events. She also argues that the issues raised by the fourth
8 cause of action are duplicative of the issues raised in a
9 separate pending state court action, and therefore, that this
10 court should abstain from deciding them.

11 The Plaintiffs respond, in essence, that the Debtor has not
12 met her burden of producing evidence negating an essential
13 element of the Plaintiffs' claims, or alternatively, of showing
14 that the Plaintiffs do not have sufficient evidence of an
15 essential element to carry their ultimate burden of persuasion at
16 trial.

17 II. ANALYSIS

18 This court has jurisdiction over the Motion pursuant to 28
19 U.S.C. §§ 1334 and 157(b)(1). The Motion is a core proceeding
20 under 28 U.S.C. § 157(b)(2)(I) and (J). The Motion was brought
21 pursuant to Federal Rule of Bankruptcy Procedure 7056, which
22 makes applicable Federal Rule of Civil Procedure 56.

23 Where a motion for summary judgment is before the court, the
24 court is to render judgment for the moving party where "the
25 pleadings, depositions, answers to interrogatories, and
26 admissions on file, together with the affidavits, if any, show
27 that there is no genuine issue of material fact and that the
28 moving party is entitled to a judgment as a matter of law." Fed.

1 R. Civ. P. 56(c). The moving party bears the burden of producing
2 evidence showing that there is no genuine issue of material fact
3 and that it is entitled to judgment as a matter of law. Celotex
4 v. Catrett, 477 U.S. 317, 322-23, 106 S. Ct. 2548, 2552 (1986).

5 Once the moving party has met its initial burden, the non-
6 moving party must show specific facts showing the existence of
7 genuine issues of fact for trial. Anderson v. Liberty Lobby,
8 Inc., 477 U.S. 242, 256, 106 S. Ct. 2505, 2514 (1986). Under
9 Rule 56, the court also has authority to make an order specifying
10 those material facts that appear without substantial controversy,
11 and such facts are deemed established for purposes of trial.
12 Fed. R. Civ. P. 56(d).

13 A. The § 523(a)(6) causes of action

14 The attorney's fee award was issued pursuant to Cal. Gov't
15 Code § 12965(b), which provides that the court has discretion to
16 award reasonable attorney's fees and costs to the prevailing
17 party in civil actions brought under the California Fair
18 Employment and Housing Act, Part 2.8 of the Government Code,
19 under which the Debtor's sexual harassment claims were brought.

20 The Debtor argues that 11 U.S.C. § 523(a)(6) applies only to
21 damages flowing from intentional torts, and not to compensatory
22 awards of attorney's fees to prevailing parties under Government
23 Code § 12965(b). This argument succeeds only if the court
24 concludes that a section 12965(b) award can never constitute a
25 form of damages for willful and malicious injury. This the court
26 declines to do.

27 The Debtor relies heavily on State Bar v. Taggart (In re
28 Taggart), 249 F.3d 987 (9th Cir. 2001). The court finds Taggart

1 to be easily distinguished from the present case. In Taggart,
2 the court held that costs awarded to the State Bar of California
3 in attorney disciplinary proceedings, pursuant to Cal. Bus. &
4 Prof. Code § 6086.10, are compensation for actual pecuniary loss,
5 rather than fines, penalties, or forfeitures, and therefore, are
6 not excepted from discharge under 11 U.S.C. § 523(a)(7). 249
7 F.3d at 994. The court found Cal. Bus. & Prof. Code § 6086.10 to
8 be analogous to Cal. C. Civ. Proc. § 1032(a)(4), (b), which
9 governs cost awards to prevailing parties in civil litigation
10 generally, because the former permits exonerated attorneys to be
11 reimbursed for the costs of defending themselves in the
12 disciplinary proceedings. Id. at 992-93. The analogy was not,
13 however, essential to the court's decision, and the decision
14 otherwise had no bearing on attorney's fees and costs awarded
15 under Gov. C. § 12965(b), and nothing whatever to do with damages
16 for willful and malicious injury under 11 U.S.C. § 523(a)(6).

17 The court notes also that after Taggart was decided, the
18 California legislature amended Cal. Bus. & Prof. Code § 6086.10
19 to provide that costs imposed under that section "are penalties,"
20 and it has been held that costs imposed under the section as
21 amended are nondischargeable under 11 U.S.C. § 523(a)(7). State
22 Bar of Cal. v. Findley (In re Findley), 2007 Bankr. LEXIS 1509,
23 at 8-10 (Bankr. N.D. Cal. 2007). That holding hardly supports
24 the conclusion that prevailing party cost awards are always
25 dischargeable.

26 More on point, but not helpful to the Debtor, is the other
27 case she cites, Dutton v. Schwartz, 21 B.R. 1014, (D. Mont.
28 1982), in which the court held that the entirety of the state

1 court judgment in that case, including the award of costs and
2 attorney's fees, arose from the willful and malicious injury, and
3 was therefore nondischargeable under 11 U.S.C. § 523(a)(6). 21
4 B.R. at 1019.

5 In Klingman v. Levinson, 831 F.2d 1292, 1296-97 (7th Cir.
6 1987), the court held nondischargeable under 11 U.S.C. §
7 523(a)(4) an award of attorney's fees agreed to in a state court
8 consent judgment in which the debtor had admitted his breach of a
9 fiduciary duty owed to the creditor. See also Florida v. Ticor
10 Title Ins. Co., 164 B.R. 636, 639 (9th Cir. BAP 1994) [attorney's
11 fees awarded by state court in action under the RICO statute, 18
12 U.S.C. § 1961, *et seq.*, held nondischargeable under 11 U.S.C. §
13 523(a)(6) as being of the same character as the underlying debt];
14 Stokes v. Vierra, 185 B.R. 341, 345, n. 5 (N.D. Cal. 1995) [if
15 actual damages awarded by state court are nondischargeable under
16 11 U.S.C. § 523(a)(2) or (4), attorney's fees awarded will also
17 be nondischargeable].

18 In her reply to the Plaintiffs' opposition, the Debtor
19 acknowledges certain other cases reaching this result, but
20 attempts to distinguish them on the basis that in this case,
21 "there is no underlying state court judgment of tortious conduct
22 to which the award of fees and costs may attach and become
23 nondischargeable." Reply to Opposition to Motion for Summary
24 Judgment, at 4:18-20.

25 A similar argument was raised and rejected in In re Sears,
26 102 B.R. 781 (Bankr. S.D. Cal. 1989). In that case, the
27 plaintiffs commenced the state court action seeking declaratory
28 relief to the effect that certain agreements with the defendant

1 were invalid. The trial court found in favor of the plaintiffs,
2 declaring the agreements to be void and awarding costs to the
3 plaintiffs, but awarding no other damages. While the plaintiffs'
4 memorandum of costs was pending, the defendant filed a bankruptcy
5 petition. At issue in the defendant's chapter 7 case was
6 "whether attorney's fees are dischargeable in bankruptcy where
7 the state court has extinguished a contract due to the debtor's
8 fraud, and where the only damages sustained are the attorney's
9 fees incurred in litigating the state court fraud action." See
10 In re Sears, 102 B.R. 781, 783 (Bankr. S.D. Cal. 1989). The
11 debtor's argument was that "since there was no underlying debt in
12 the declaratory relief action, the ancillary debt [for attorney's
13 fees] has nothing to cling to and therefore is dischargeable."
14 See ibid.

15 The court agreed that the attorney's fees were not ancillary
16 obligations, but "are in the nature of a primary debt," which was
17 "the direct and proximate result of the fraud perpetrated by
18 defendant." 102 B.R. at 784. "As California law has
19 consistently awarded attorney's fees in a rescission action, the
20 attorney's fees incurred are the damages suffered by plaintiffs
21 and constitute the primary or underlying debt." Ibid.

22
23 It is absurd to suggest that had the superior court
24 awarded one dollar to plaintiffs as damages their
25 attorney's fees would be non-dischargeable, but since
26 no dollar award was made the attorney's fees should be
27 dischargeable. Nor would it make sense to require a
28 creditor to wait until a payment is made under a
fraudulent contract before bringing an action for
rescission. Equity requires this court to rule that
the attorney's fees incurred in the state court
litigation are non-dischargeable.

102 B.R. at 785.

1 Similar considerations pertain here. At the time the
2 Debtor's bankruptcy case was commenced, the Plaintiffs in this
3 adversary proceeding were prosecuting a malicious prosecution
4 action against the Debtor in state court. In that action, they
5 allege that the Debtor's prosecution of the underlying sexual
6 harassment claims was willful and malicious, and resulted
7 directly in damages in the form of the attorney's fees and costs
8 the Plaintiffs expended in defending themselves, as embodied in
9 the attorney's fee award. If the Plaintiffs are successful in
10 that action (and if the court's findings and conclusions are
11 sufficient), or if they succeed in this adversary proceeding in
12 proving that the Debtor's conduct was willful and malicious
13 within the meaning of section 523(a)(6), the attorney's fee award
14 will be nondischargeable.

15 The Debtor points out that the only jury award for the
16 Plaintiffs in the original state court action was on their
17 trespass to chattels claim, on which the jury specifically found
18 that the Debtor had not acted with malice or oppression. The
19 Debtor also notes that the state court entered no judgment
20 against the Debtor for an intentional tort. However, it remains
21 to be seen whether the Debtor committed an intentional tort in
22 prosecuting the sexual harassment claims. If she did, the
23 attorney's fee award would be nondischargeable, because it was a
24 direct result of that conduct.

25 The Debtor also argues that the trial judge's findings in
26 his order awarding the attorney's fees were merely *dicta*, and
27 therefore, are not binding on this court. Assuming for the sake
28 of this decision only that this is accurate, it remains to be

1 seen whether this court or the state court will determine that
2 the Debtor's conduct in prosecuting the sexual harassment claims
3 was willful and malicious.

4 Finally, the Debtor contends that certain remarks made by
5 the Plaintiffs in their state court appeal brief are an admission
6 that the attorney's fee award was compensatory, and "not a
7 penalty and not akin to punitive damages." Debtor's memorandum
8 of points and authorities, at 9:15-17. Again, this misses the
9 mark. For purposes of section 523(a)(6), the question is not
10 whether an award is compensatory or punitive, but whether it
11 flows directly from willful and malicious conduct. Indeed,
12 damage awards for willful and malicious injury are almost
13 invariably compensatory in nature, with punitive damages awarded
14 in certain circumstances. The absence of a punitive damage award
15 does not render compensatory damages dischargeable. See, e.g.,
16 Carillo v. Su (In re Su), 290 F.3d 1140 (9th Cir. 2002)
17 [remanding for consideration of malice issue; state court
18 judgment included \$130,000 in economic damages and \$400,000 in
19 non-economic damages, but no punitive damages].

20 For these reasons, the court concludes that the attorney's
21 fee award is a direct result of the Debtor's conduct in
22 prosecuting the sexual harassment claims. Whether that conduct
23 was willful and malicious, within the meaning of 11 U.S.C. §
24 523(a)(6), remains to be seen.

25 B. The § 727(a) causes of action

26 1. The third cause of action

27 In the third cause of action of the Complaint, the
28 Plaintiffs contend that the Debtor failed to keep or preserve the

1 following records from which her financial circumstances might be
2 ascertained: records relating to (1) her debt to the law firm of
3 Brayton Purcell, (2) her possible causes of action against
4 Brayton Purcell for malpractice, and (3) "the pursuit of the
5 malicious prosecution action against Brayton Purcell and Clayton
6 Kent." Complaint, at 5:23-25.

7 The Debtor addresses only the first of these points in her
8 Motion, and on that point, the court concludes that there are
9 genuine issues of material fact remaining to be decided. First,
10 the Debtor testifies in her supporting declaration that she
11 "never received any billings, demands or requests for payment
12 from Brayton Purcell;" she argues, in essence, that she could not
13 keep or preserve what she did not receive. Her deposition
14 testimony was far more equivocal on this point.

15 Q. What efforts did you make to ascertain whether or not
16 you had such documents?

17 A. First of all, I don't recall ever having any so, you
18 know, not knowing if I ever had any to begin with, I didn't
19 really know how to go around looking for something I never
20 even knew if I had in the first place.

21 Plaintiffs' Exhibit N in support of their opposition to the
22 Motion, at 4 (page 13 of the deposition transcript).

23 Second, the Debtor has submitted a declaration of her
24 attorney, Thomas P. Griffin, Jr., in which he states that an
25 attorney at Brayton Purcell told him the firm does not have any
26 documents responsive to the Plaintiffs' subpoena for these

27 / / /

28 / / /

1 records, except a retainer agreement.³ Assuming this hearsay
2 statement is admissible, it does not support the conclusion that
3 there are no genuine issues of material fact with respect to the
4 Debtor's alleged failure to keep or preserve appropriate records.

5 2. The fourth cause of action

6 In their fourth cause of action, the Plaintiffs complain
7 that the Debtor, with intent to hinder, delay, or defraud
8 creditors, concealed property of the Debtor within the year
9 before the date of filing of her bankruptcy petition.
10 Specifically, the Debtor is alleged to have "intentionally
11 conspired to provide services to her employer for a salary which
12 was substantially less than the value of those services."
13 Complaint, at 6:7-9.

14 The Debtor argues simply that she has disclosed all of her
15 income, and that her version of the circumstances as to the
16 changes in her income is the accurate one. In order to grant the
17 Motion as to this point, the court would have to accept the
18 Debtor's version of events as true, accept the inferences she
19 draws therefrom, and reject the testimony of other witnesses and
20 inferences that might be drawn from the documentary evidence.
21 The same may be said of the Debtor's response to the Plaintiffs'
22 argument that she has kept insufficient records of her expenses.
23 In short, the arguments on both sides of these issues reveal that
24 / / /

25 _____
26 3. The Debtor characterizes this as a statement that "Brayton
27 Purcell, LLP never sent a billing statement, demand or request for
28 payment to the Debtor." Debtor's memorandum of points and
authorities, at 11:11-17, 11:21-22. Counsel's declaration does not
show that such records were never sent to the Debtor, only that
Brayton Purcell claims it does not have such records.

1 there are a host of genuine issues of material fact remaining to
2 be decided.

3 Finally, the Debtor contends the issues raised in the
4 Plaintiffs' fourth cause of action are also the subject of
5 pending state court litigation, and therefore, that this court
6 should abstain from deciding them. The pending litigation is an
7 action by the Plaintiffs against the Debtor and her husband and
8 employer, Marc Hughes, to recover the value of fraudulent
9 transfers allegedly made by the Debtor to Mr. Hughes in
10 connection with alleged shifting of income and expenses.
11 Assuming the automatic stay does not prevent the Plaintiffs from
12 proceeding with the state court litigation, the difficulty with
13 the Debtor's argument is that the remedies sought in the two
14 actions are entirely different. In this adversary proceeding,
15 the Plaintiffs seek to deny the Debtor's bankruptcy discharge,
16 which is a matter within this court's exclusive jurisdiction.
17 Accordingly, there is no basis for this court to abstain from
18 determining whether the Debtor is entitled to a discharge.

19 III. CONCLUSION

20 For the reasons set forth above, the court will issue an
21 order denying the Motion.

22
23 Dated: July 10, 2007

Robert S. Bardwil

24 ROBERT S. BARDWIL
25 United States Bankruptcy Judge
26
27
28

Certificate of Service

I certify that on JUL 10 2007 a copy of the foregoing
document was mailed to the following:

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FOR THE COURT
RICHARD G. HELTZEL
CLERK, U.S. BANKRUPTCY COURT

By: 

Deputy Clerk